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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

IN THE MATTER OF	)	
	)	
AMENDMENT OF PART 36 AND PART 69	)	
OF THE COMMISSION'S RULES TO	)	RM-
EFFECT COMPREHENSIVE REFORM OF THE	)	
ACCESS CHARGE SYSTEM	)	

PETITION FOR RULEMAKING
OF THE
AD HOC TELECOMMUNICATIONS USERS COMMITTEE

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April 15, 1994

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Summary

In this Petition the Ad Hoc Telecommunications Users Committee presents a program for transitioning toward fundamental Part 69 access charge and Part 36 separations reforms that the Committee believes are essential to keep pace with legislative, technological and marketplace changes and, concurrently, provide a regulatory environment within which competitive opportunities will be maximized.

The Committee believes that without basic reform of existing subsidy flows in a way that preserves clearly defined universal service objectives while, at the same time, moving toward more efficient, cost based recovery methods, attempts to achieve effective access charge system reform are essentially futile. Therefore, the Committee's proposal calls for initial focus on reform of uneconomic subsidies, including both direct subsidy flows under the current universal service funding mechanisms, and indirect subsidies embodied in the current Part 36 separations procedures. The Committee also proposes an interim procedure featuring de-linkage of Part 36 and Part 69 categories that will allow for initial Part 69 access charge reform to commence. Certain elements of access charge reform, such as according LECs additional pricing flexibility, however, must be geared toward marketplace conditions and await emergence of effective levels of competition.

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PETITION FOR RULEMAKING
OF THE
AD HOC TELECOMMUNICATIONS USERS COMMITTEE

The Ad Hoc Telecommunications Users Committee ("Ad Hoc Committee" or "Committee"), pursuant to Section 1.401 of the Commission's Rules, hereby petitions for initiation of a rulemaking looking toward amendment of provisions of the Commission's rules under Part 36 (Jurisdictional Separations Procedures) and Part 69 (Access Charges) as necessary to implement comprehensive reform of the Access Charge System.[1/]

I. INTRODUCTION

As a consistent proponent of the benefits of competition in the provision of telecommunications services and products, the Ad Hoc Committee is vitally interested in seeing that the Commission's rules governing interstate access services keep pace with legislative, technological and marketplace changes, and that the access charge rules are revised in such a way as to best promote competition in the provision of exchange access and local exchange services, as well as in any new

[1/] As used in this petition, the term "Access Charge System" encompasses the access charge structure, jurisdictional separations, universal service funding, and pricing rules.

services which may evolve as part of the National Information Infrastructure. The Ad Hoc Committee believes that realization of this objective will require a careful balancing of interests and a coordinated program for transitioning toward fundamental access charge and separations reform. The Ad Hoc Committee presents in this petition a specific program of interim rule revisions and longer-term transitions designed to minimize disruptions while ultimately achieving broad Access Charge System reform objectives in a balanced and orderly fashion.[2/]

II. COMPREHENSIVE ACCESS CHARGE SYSTEM REFORM IS NEEDED TO ENSURE A BALANCED AND ORDERLY PROCESS FOR TRANSITION TO EFFECTIVE COMPETITION

The number of access reform proposals now before the Commission, and the wide range of interest and industry comment they have generated, appear to reflect a general consensus that changes in the now ten-year old access charge rules are required.[3/] There also seems to be general agreement that the goal of access charge reform should be to move toward more cost-

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2/ This petition is based upon Access and Competition: The Vital Link, March, 1994, prepared for the Committee by Economics and Technology, Inc. (the "ETI Report"). This paper, a copy of which is attached as Exhibit A, provides full detail of the Committee's proposed program for overall reform of the Access Charge System.

3/ See, In the Matter of Petition For Declaratory Ruling And Related Waivers to Establish a New Regulatory Model for the Ameritech Region, DA 93-481, released April 27, 1993; In the Matter of NARUC Petition For Notice of Inquiry Addressing Access Issues, DA 93-847, released August 3, 1993; Federal Perspectives on Access Charge Reform, A Staff Working Analysis, April 30, 1993; In the Matter of Amendments of the Rules to Reform Interstate Access Charges: USTA Petition for Rulemaking, Public Notice (Report No. 1975), released October 1, 1993.

based pricing of access services[4] and, as actual levels of emerging competition may warrant, increasing LEC pricing flexibility.[5] The real question is in the transition: how best to structure access reform to get from here (niche competition) to there (effective competition). The Ad Hoc Committee is of the view that Part 69 access reform will promote development of competition only if done on a comprehensive basis so as to effect coordinated changes in the Access Charge System as a whole. In other words, because of the close interrelationship between the Part 69 access charge rules, universal service funding mechanisms, jurisdictional separations procedures, and access pricing (i.e., price cap regulation), effective access charge reform must include complementary reforms in, or coordination with, each of these areas.[6] In contrast, certain of the pending proposals recommend a piecemeal approach to access reform, such as according LECs additional pricing flexibility without overall reform of the existing, underlying system. The

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[4] Although the Ad Hoc Committee agrees that the overall goal of reform of the Access Charge System should be a more cost-based access pricing environment, this must be done in a way that does not inappropriately disadvantage competitors.

[5] There is, of course, substantial disagreement over the level of existing competition and, as a consequence, the appropriate timing of allowing LECs further pricing flexibility. However, by definition, the cost-based rate goal requires abandoning any vestige of historic access charge objectives aimed at protecting LEC revenue sources.

[6] Among specific illustrations of interrelationships discussed in the ETI Report: the current separations system's assignment of NTS costs to the TS access service category; and, state-approved infrastructure modernizations being automatically flowed through to interstate access services.

Committee believes that such one dimensional approaches will not achieve the Commission's objectives of promoting competition and realizing more cost based pricing of access services.

The Ad Hoc Committee also believes it to be essential that comprehensive reform of the Access Charge System proceed as soon as possible. To some extent, this represents a departure from the Committee's past opposition to proposals calling for a general overhaul of the access charge rules,[7] and reflects the Committee's belief that changing competitive, legislative and technological circumstances, combined with the danger that only certain facets of the current access charge policy might be addressed in isolation as suggested by some of the pending access reform proposals, require the Commission to move quickly to initiate an overall reform process.

The Ad Hoc Committee continues to support transitional change in the Access Charge System, but has reached the conclusion that a framework for an overall reform process must be established at the outset by the Commission to ensure a balanced and orderly transition. The Committee also continues to believe that effective access charge reform is not feasible without fundamental jurisdictional separations reform (and continues to propose that the Commission's initial focus be on separations reform), but has modified its previously expressed view that full separations reform must be implemented before the Commission

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[7] See, Comments of Ad Hoc Telecommunications Users Committee filed November 1, 1993 in response to USTA Petition for Rulemaking in RM-8356.

initiates significant access reform. Instead, the Committee proposes that separations and access reform proceed on parallel tracks under a coordinated program that allows for incremental rule changes as the exchange access and local exchange markets evolve. Such a program would alleviate concerns previously expressed by the Committee that a comprehensive access reform undertaking might "bog down" progress in the Commission's Expanded Interconnection, Transport Rate Structure, and Intelligent Network Proceedings wherein the Commission seeks to further open these markets to competition. As detailed in the ETI Report, the Ad Hoc Committee offers a roadmap for Access Charge System transitional change intended to minimize disruption, achieve a balance among disparate interests (including those of the LECs), and maximize opportunities for growth in competition.

III. REFORM OF EXISTING SUBSIDY MECHANISMS IS AN ESSENTIAL PREREQUISITE TO EFFECTIVE ACCESS CHARGE SYSTEM REFORM

Efforts to implement broad access charge reform without first addressing the direct, or explicit, subsidies flowing under current universal service funding mechanisms, as well as the indirect, or implicit, subsidies flowing under the Part 36 jurisdictional separations procedures, are inherently futile and potentially counterproductive to achievement of the cost-based pricing and pro-competitive goals sought to be realized by the Commission. As stated in the ETI Report:

> While not all parties may agree with our prescriptions for comprehensive access reform, we nevertheless believe that we are offering a logical sequence for initiating the access

> reform process. The Committee proposes that the Commission first focus upon jurisdictional separations reform and upon eliminating remaining inefficiencies (i.e., non-cost based recovery methods) found in the access charge rules, while ensuring that adequate mechanisms for support of universal service objectives are maintained. Major access reform issues relative to pricing flexibility can begin to be addressed, but full pricing flexibility should await separations and basic access efficiency reforms, and should be timed to relate to the emergence of effective competition for specific access services.[8/]

The Ad Hoc Committee recognizes that the Commission's jurisdictional limitations circumscribe the effectiveness of actions it may take unilaterally and that, to be fully effective, reform of existing subsidy mechanisms must proceed at the state level as well.[9/] However, the Commission may lead by example. Initiation of the approach proposed in this petition will materially assist in setting in motion a process for overall subsidy mechanism reform.

A. Reform of Universal Service Funding

The Ad Hoc Committee believes that any plan for reform of the Access Charge System must make adequate provision for, and continued assurance of, universal service, and that perpetuation of some arrangement for accomplishing the results of existing

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8/ ETI Report, p. 8.

9/ For example, whereas approximately three-fourths of interstate-assigned NTS costs are being recovered appropriately through fixed monthly end user (SLC) charges, a far lower percentage of state-assigned NTS costs is being recovered in this manner. Thus, even if the CCLC were eliminated entirely at the federal level, in the aggregate a substantial portion of NTS costs would continue to be recovered through usage-based rate elements applied to local and intrastate toll services, and to intrastate switched services.

"exchange-level" (i.e., Universal Service Fund) and "low-income subscriber level" (Lifeline and Link-Up programs) subsidization mechanisms must be a key component of any reform of the Access Charge System. At the same time, the Committee believes that current methods of universal service funding must be critically re-examined and a new funding scheme designed that will be as neutral in its effects upon demand and competition as possible. In particular, the role of subsidy and assistance mechanisms in a reformed access charge structure should be kept to the minimum necessary to efficiently accomplish public policy goals and, equally as important, reformed mechanisms must be designed so that they cannot be employed to subsidize LEC operational inefficiencies or non-market based investments, or to protect LECs from competitive incursions and loss of market share. Specifically, the Ad Hoc Committee proposes that a universal service policy for an increasingly competitive environment should serve the following goals: create a mechanism for determining and for delimiting where subsidies should be applied; establish how much subsidy is appropriate for each situation; determine how the subsidy will be funded; and, establish a mechanism for impartially administering the collection and distribution of such subsidies.

Toward these ends, the ETI Report offers the following proposals for universal service funding reform:

- Base funding for universal service upon the existing definition of basic service until such time as there is demonstrated customer demand for broadband service that would meet a threshold test for measuring such demand

and warrant expansion of the definition. Acquisition of new network resources should be driven by demand, not government fiat, and accomplished through a fully competitive process (i.e., not through unilateral diversions of monopoly services revenues by dominant LECs).

- Because the existing "exchange-level" subsidization process fails to distinguish between the "high cost" attributes of the serving area itself and the inefficiencies inherent in non-competitive provision of service, allow competing access providers to bid for service to "high cost" exchanges and to include in their bids an amount for high cost support (thereby improving overall economic efficiency and lowering the size of the fund). Provide for mechanisms to protect telephone subscribers in the event an unqualified provider bids for and receives the right to receive subsidies.[10/]

- Collect USF funds through as assessment against loop facilities provided by all local service providers, including competitive access providers, rather than collecting from IXCs on the basis of presubscribed lines.

- Collect and distribute USF funds through a neutral non-service provider party, rather than through NECA.

Overall, the Ad Hoc Committee advocates a "zero-based" approach to both the explicit subsidies found in the Commission's universal service funding mechanisms and to the implicit subsidies inherent in the existing separations procedures. A "means" test should be developed to size and target any subsidy.[11/] Having thus determined and delimited subsidies

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10/ The Commission should also examine the generally accepted notion that LECs are "burdened" by universal service obligations, and should consider the competitive benefits which may be derived by LECs due to the ubiquity attached to the universal service obligation.

11/ For example, the evidence relative to subscriber "drop-off" as SLC levels have increased suggests the price elasticity of demand for the vast majority of residential customers is (continued...)

directly serving explicit public goals, the Commission then should adopt a mechanism that requires all providers of local service to contribute equitably. While it is inappropriate that only LEC services be subject to contribution obligations in support of universal service or other public interest goals, it is equally inappropriate that the traditional structure of LEC costs and markets, including the inefficiencies in these structures, be imposed on competitor services through the need to conform to subsidy requirements.

B. Separations Reform

The overall level of revenue requirement allocated between the federal and state jurisdictions by the separations process is directly affected by the scope and definition of universal service. In turn, the extent to which Part 69 access charge rules can be reformed is directly affected by how the separations system allocates the revenue requirement. In addition to the explicit subsidies provided through universal service funding mechanisms, there are numerous implicit subsidy flows inherent to the overall pricing of telecommunications under the current separations system whereby certain services are priced well in excess of costs while others are priced so as to make no or minimal contribution to fixed overheads and common

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[11] (...continued) virtually zero. Therefore, not each and every residential subscriber requires subsidized basic service.

costs.[12] Thus, separations drives access policy, and there can be no serious examination of access reform without first moving towards resolving inefficiencies in the underlying process by which costs are assigned to and recovered from the respective state and federal jurisdictions. And, until uneconomic cost recovery methods endemic to the existing separations process are addressed and remedied, access costs can not be recovered in an economically efficient manner and comprehensive access reform is impossible.

Most industry observers would agree that current separations practices do not provide meaningful and accurate cost information for either the state or the interstate jurisdictions. The Ad Hoc Committee believes that the basic goal of separations reform should be to create a jurisdictionally transparent system that promotes efficient and consistent pricing, rather than arbitrarily assigning jurisdictional responsibility for pricing decisions or constraining economic pricing policies by arbitrary cost classifications. There are two distinct areas in which these problems should be addressed: the mechanism used to allocate costs (revenue requirement) between the jurisdictions and between traffic-sensitive and non-traffic-sensitive categories; and, the overall level of revenue requirement being assigned to the interstate jurisdiction.

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[12] These subsidies include below cost pricing of basic residential access and subsidy flows from relatively low cost service areas to above average cost areas.

To address the "mechanism" problem, an entirely new results oriented approach is needed. Toward this end, the Committee has refined its previously proposed "MART" system[13] to better reflect current and future technology and market conditions, and offers the Jurisdictional Transfer Mechanism ("JTM") discussed in further detail in the ETI Report. JTM would approach jurisdictional separations from the standpoint of desired policy goals, implementing a system of revenue transfers designed to support and achieve those goals. This system would eliminate arbitrary NTS cost assignment practices, such as the current 25 percent "fixed" assignment to the federal jurisdiction, and remedy putatively economic-based assignments of TS costs which, although based on relative use, effectively assign disproportionate costs to the interstate jurisdiction. JTM would also address the problem of the excessive overall level of revenue requirement assigned to the federal jurisdiction. The existence of this excessive federal revenue requirement was confirmed by the Commission's decision to create the so-called "residual interconnection charge" in the Transport Rate Structure Proceeding.

In the same way that separations has driven the existing access charge rules, the process of separations reform should be structured to facilitate access charge reform. Rather

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[13] The "Minimal Annual Revenue Transfer", or MART, system was submitted by the Ad Hoc Committee to the NARUC Access Industry Work Group, and later discussed in the Committee's Comments on the NARUC Petition for Notice of Inquiry Addressing Access Issues, filed September 2, 1993.

than attempting to effect incremental repairs or "quick fixes" to a separations process that is inherently flawed, JTM concentrates on the end results of the cost allocation process with a focus on an annual interstate revenue requirement for each LEC. The JTM approach offers a far more simplistic and effective alternative, replacing a system dominated by minutia and a multiplicity of allocation factors with a process that looks to end results, or overall revenue requirements, rather than detailed and increasingly outmoded cost categories. Thus, unlike current separations practices, under a JTM approach, the costs associated with new network technologies would not be distorted by technologically obsolete cost categorization rules.

IV. ACCESS REFORM MAY MOVE FORWARD IN A PARALLEL PROCEEDING IF "DE-LINKED" FROM PART 36 CATEGORY-BY-CATEGORY COST ASSIGNMENTS

Recognizing that broad separations reform is apt to prove a long and contentious process, and in order to move forward to the extent possible with access reform during the course of this process, the Ad Hoc Committee proposes that the Commission, as an initial interim step, de-link the Part 36 Jurisdictional Separations Rules from the Part 69 Access Charge Rules. Under this interim arrangement, the Access Charge Rules would continue to rely on the Separations Rules only for the development of a bottom line, total interstate revenue requirement. Just as state regulators use separations results for the development of an overall revenue requirement, reaching rate making decisions based on factors such as marginal costs and public policy objectives, the Commission need not base interstate rate making decisions upon category-by-category results of Part 36 assignments of revenue requirement. The existing separations system necessarily flows through into the access charge environment all of the uneconomic cost assignment and other flaws inherent in that system, making efforts at overall access charge reform essentially futile. By adopting an interim procedure that de-links category-by-category assignments, the Commission can move forward with separations and access charge reform concurrently in two parallel rulemakings, leaving the Commission free to develop access service prices in a more economically efficient manner even before the separations reform rulemaking is completed.

The proposed interim procedure will allow the Commission to proceed at once to implement significant revisions in the current access charge rate structure so that access rates track underlying costs more closely.[14/] However, other issues should be addressed only when justified by market and technological developments. Among the latter is the question of affording LECs "full" pricing flexibility or, for that matter, further elements of pricing flexibility beyond those already

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[14/] Such changes would include implementing usage based recovery of certain traffic sensitive costs currently recovered uneconomically as NTS costs, and adjusting costs recovered on a more distance sensitive basis than actual patterns of usage would support. In addition, the Commission should uncap the EUCL for the general body of residential and single line business customer, transitioning toward costs, and lower the CCLC as the EUCL increases.

provided under price cap regulation and zone density pricing. The Ad Hoc Committee would support more substantial levels of LEC pricing flexibility when effective competition in the provision of exchange access and local exchange services becomes reality. However, premature LEC pricing flexibility could destroy emerging competition or, alternatively, prevent the local exchange and access markets from witnessing otherwise achievable levels of competition.

Finally, while not part of the formal "access charge reform" process, the Commission should consider the effect on competition of pricing flexibility issues which may be raised in the current Price Cap Review Proceeding (CC Docket No. 94-1) in the context of overall Access Charge System reform.

V. CONCLUSION

The Commission should proceed with Access Charge System reform through issuance of a notice of proposed rulemaking initiating a balanced and orderly process of transition as proposed in this petition and in the ETI Report.

Respectfully submitted,

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EXHIBIT A

ACCESS AND COMPETITION: THE VITAL LINK

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Prepared for the
Ad Hoc Telecommunications Users Committee

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ACCESS AND COMPETITION: THE VITAL LINK

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Access and Competition: The Vital Link

Lee. L. Selwyn and Susan M. Gately*

I. Introduction

The current "Access Charge System" as codified in Part 69 of the FCC's Rules,[1] was created in the aftermath of two seminal judicial events — the 1978 *Execunet* decision[2] that established the right of new entrants to compete with AT&T in the provision of interstate long distance service, and the 1984 implementation of the *Modification of Final Judgment* (*MFJ*) that settled the Justice Department's 1974 antitrust suit against AT&T.[3] The two *judicial* events provided bookends around the FCC's initial effort at establishing a system of "access charges" to provide compensation to local exchange carriers (LECs) for their participation in the origination and/or completion of long distance calls and, in particular, to preserve at least some of the historic subsidy from long distance revenues to the basic subscriber access line ("loop") while transitioning to a more cost-based pricing structure.[4]

The goals of the initial access charge system were both limited and pragmatic: The Court in *Execunet* had remanded the matter of implementation of long distance competition back to the FCC, which was (albeit slowly and methodically) progressing toward some sort of access charge system when, in January, 1982, a time frame for closure was

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*. The authors are, respectively, President and Vice President of Economics and Technology, Inc, One Washington Mall, Boston, MA 02108. The authors gratefully acknowledge the contributions and helpful comments of James S. Blaszak in the preparation of this paper.

1. 47 CFR § 69

2. *MCI Telecommunications Corp. v. FCC*, 561 F.2d. 365 (D.C. Cir., 1977) ("Execunet I") *cert. denied* 434 US 1040 (1978); *Mandate issued* 580 F. 2d 590 (D.C. Cir.) ("Execunet II") *cert. denied* 439 US 980 (1978).

3. *United States v American Tel. & Tel. Co.*, 552 F. Supp. 131, 226, 227 (D.D.C 1982) (*"Modification of Final Judgement"* or *"MFJ"*), *aff'd sub nom.* Maryland v. United States, 460 U.S. 1001 (1983).

4. *See generally* MTS and WATS Market Structure, CC Docket No. 78-72, *Notice of Inquiry and Proposed Rulemaking*, 67 FCC 2nd 757 (1978). *Supplemental Order (Phase I)*, 94 FCC 2nd 852 (1983). *Phase I Order Modified on Reconsideration*, 97 FCC 2nd 682 (1983). *Phase I Order Modified on Further Reconsideration*, 97 FCC 2nd 834 (1984). Phase I Orders Affirmed in Part, *Remanded in Part sub nom. National Association of Regulatory Utility Commissioners v. FCC*, 737 F.2d 1095 (D.C. Cir. 1984). *Cert. denied*, 469 U. S. 1227 (1985). *Report and Order (Phase III)*, 100 FCC 2nd 860 (1985). *Phase I Order Modified on Second Further Reconsideration*, 101 FCC 2nd 1222 (1985. *Aff'd sub nom. American Telephone & Telegraph Co. V. FCC*, 832 F.2d 1285 (D.C. Cir. 1987).

externally imposed on the FCC by the January, 1984 implementation date for the break-up of the Bell System. At that time, the focus of policy was on separating the "competitive" long distance market from the "monopoly" local market, and for assuring that competing providers of long distance service — none of whom would be affiliated with the local service monopolies — could be assured the unimpeded availability of efficient and equal interconnections at cost-based prices.

While the LECs' *de facto* monopoly is still largely intact,[5] the entry of limited competition at the LATA level — together with a decade of experience and maturity under the "first generation" of access charges — has introduced a new dimension and a new focus into access charge policy at both the federal and state levels. IntraLATA toll competition is now or will soon be permitted in most states;[6] so-called "competitive access providers" ("CAPs") have begun serving selected high-volume users and interexchange carriers in more than 50 cities; and several cable television operators have announced plans to introduce residential/small business "dial tone" service to compete directly with LEC-provided subscriber access lines.[7]

It should thus come as no surprise that considerable momentum is now building for a fundamental reform of the US access services environment. But while most stakeholders agree that reform is necessary, there is considerable *disagreement* as to the manner — and the pace — of such reform. In that context, it is essential that the FCC develop an

5. In 1992, LECs earned more than $25.7-billion in access charge revenues; all other "competitive" access providers *combined* generated access charge revenues of only about $209-million, giving the LECs a 99.2% share of the national access services market. *Local Telecommunications Competition: 1993 ("The ALT Report")*, Connecticut Research, P.O. Box 1379, Glastonbury, CT 06033, Table I-2.; *Statistics of Communications Common Carriers*, Federal Communications Commission, 1991/1992 Edition, p. 236.

6. See *State Telephone Regulation Report*, September 9, 1993, pp. 1-6 (Eastern states) and September 23, 1993, pp. 1-7 (Western States, including Alaska and Hawaii). Facilities-based intraLATA competition for all interexchange services presently exists in more than 40 states.

7. As of this writing, no commercially-available competitive dial tone service is available from cable television operators anywhere in the US, with the exception of very limited "trials" in a handful of cities. However, in the UK, several cable television systems — including some that are partially owned by US Regional Bell Holding Companies — are currently offering such services in direct competition with British Telecom. In fact, NYNEX holds stakes in 11 U.K. cable TV franchises. See "British Welcome RHC Cable Participation, But Blast 'Restrictive' U.S. Market-Entry Policies; NYNEX says U.K. Cable Ventures Are Neither 'Altruistic' Nor 'Experimental,' *Telecommunications Reports*, Vol. 57, No. 10 at 9. Despite the widely acclaimed success of the cable-provider entries in the U.K. local exchange market, the incumbent provider still dominates: it has been estimated that cable companies may capture 20% of the market within ten years, meaning that the incumbent LEC would still provide service to 80% of all subscribers. (See, *Wired Planet*, THE ECONOMIST, Feb 12, 1994, at Survey 13.

affirmative plan for the reform of the Access Charge System[8] that appropriately balances these various interests and concerns. Unlike the situation preceding the 1984 Bell System break-up, there is no specific event that externally imposes a schedule for completion of this process; there is no fast-moving train bearing down on the FCC that would require the type of pragmatic trade-off of expediency and simplicity for fundamental economic efficiency. Moreover, and unlike the world prior to the break-up, the country has become sensitized to greater competition and complexity in the telecommunications marketplace, and to the "rebalancing" of usage-sensitive network services charges and non-traffic-sensitive subscriber access charges to better reflect their underlying economic costs. Long distance rate levels available to individual consumers have declined by nearly 50% in nominal terms since their pre-MFJ levels,[9] and close to 93% in *real* terms.[10] This new climate is conducive to a well-reasoned and comprehensive review of federal access charge policy and to the ultimate adoption of efficient prices that can be driven by economics rather than by politics, by current policy goals of encouraging the development of effective competition where feasible and efficient rather than by the former goal of protecting historic LEC revenue sources. In short, the FCC now has the opportunity to benefit from a decade of experience and to craft a new and effective mechanism for achieving and for maintaining current policy goals.

This paper details specific recommendations for a Notice of Proposed Rulemaking concerning fundamental access charge and separations reform. It proposes a program of revisions and transitions that are designed to minimize disruptions while ultimately achieving the broad reform objective and balance.

II. The Need for Fundamental Reform

The present momentum for reform of the access charge system is being driven by a number of conditions and events, principal among which are these:

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8. As used herein, the term *access charge system* encompasses access charge structure, separations, universal service funding and pricing rules.

9. This relationship is based upon a comparison of by-the-call interstate MTS rates in 1983 (the only tariff available to individual consumers and small businesses) to "block of time" type pricing options, with a minimum usage level of one hour per month, that are offered by AT&T ("Reach Out America"), MCI ("Prime Time"), or Sprint ("The Most").

10. During the time period of this 50% decrease in *nominal* prices, inflation actually increased by some 43% as measured by the Fixed Weight Gross Domestic Product Price Index (GDP—PI) for 1983 to 1993. (*Economic Report of the President*, Washington, D.C., U.S. Government Printing Office, February, 1994, Table B-4, page 274.) The 50% decrease in the face of a 43% increase in inflation yields the 93% decrease in *real* (i.e., inflation-adjusted) dollars.

- *Competition, competition, competition* — existing and potential competition in the interexchange, access, and local service markets is causing both entrenched providers as well as present and future competitors to call for changes in the existing system. "Reform" proposals of one type or another have been advanced by Rochester Telephone Corporation, by Ameritech and by NYNEX in 1993: All three of these plans are indicative of the types of "quick-fix" reform schemes that are likely to be pushed by many LECs unless there is positive FCC movement toward *overall* reform of the existing underlying system.[11]

- *Interrelationships among Access Charge System components* — all of the access charge system elements (separations, universal service funding, Part 69 access rules, and price caps review) are closely interrelated — a change in any one segment either is impacted by, or limits, each and every other one. Even seemingly unrelated issues, such as state-approved infrastructure modernization and upgrade plans, tie into this picture.

  As an example, it is now widely accepted that the existing separations system attributes to the traffic-sensitive access service category certain cost sources (revenue requirement) that are in reality not traffic-sensitive.[12] As a result, the access pricing rules cannot be reformed to allow traffic-sensitive prices to more closely track traffic-sensitive costs because those prices must also recover that portion of the *non-traffic-sensitive* (NTS) revenue requirement that has been (erroneously) assigned there by separations. (See discussion of Part 69.106 in *Section VI (Separations Reform)* below.)

  Similarly, revenue requirement increases driven by state-approved infrastructure modernization plans are automatically flowed through to interstate access services, particularly traffic-sensitive services, through the workings of the separations and access charge rules. Therefore, even infrastructure plans that might be limited, for example, to the deployment of fiber facilities to schools, could result in increases in the interstate switched access revenue requirements. In the future it is possible that approval of such plans will result in additional draws upon the universal service and high cost funds as well.

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11. Support for this expectation is found in the language of the waiver request associated with NYNEX's *Universal Service Preservation Plan*. In that request, NYNEX indicates that the "unique" circumstances that it faces, that require it to depart from the existing access structure, are unique to NYNEX only in terms of degree and timing. NYNEX bases its request for pricing reform on the fact that competition has developed more quickly in its territory than in other parts of the country.

12. See Comments of the Coalition of Open Network Architecture Parties ("CONAP"), *In the Matter of Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelement for Open Network Architecture (CC Docket No. 89-79)*, filed August, 1989.

- *Telecom legislation is presently pending on Capitol Hill*[13] — passage of any of the pending bills in some form could have a dramatic impact upon all elements of the access charge system, serving if anything to accelerate the need for a well-thought-out approach to these issues. Passage of any of these pieces of legislation will result in *structural* changes to the competitive landscape. The already antiquated access charge and separations rules are not sufficient to deal with the new environment that may emerge and evolve in the coming years.

- *Rapid pace of technological change* — technological changes impact both access service costs and the potential for competition in the access environment. These changes are occurring at an ever more rapid pace, making the need for reform of all access charge system pieces more crucial than ever.

Although the industry environment is rapidly changing and revisions to certain facets of current access charge policy are being sought immediately, e.g., through so-called "waiver requests" applied for by NYNEX, Ameritech and perhaps others, this kind of piecemeal approach to access charge reform can only exacerbate the problem in the future by failing to address fundamental, threshold questions *now*. Moreover, while some aspects of the reforms being sought through waivers may have merit, others are self-serving and transparent: For example, as the Ad Hoc Committee noted in its Comments filed January 31, 1994 to the NYNEX waiver petition,[14] one key parameter of the NYNEX formula is a measure of *national* market share. If as a result of current legislative initiatives NYNEX and the other RBHCs are permitted to offer interLATA services, NYNEX is likely to have a disproportionately high market share *in-region* than nationally,[15] and any access charge

13. *See* proposed H.R. 3626, "Antitrust Reform Act of 1993," ("Brooks-Dingall Bill"); *see also* proposed H.R. 3636, "National Communications Competition Infrastructure Act of 1993," ("Markey-Fields Bill").

14. See NYNEX Petition for the Transition Plan to Preserve Universal Service In A Competitive Environment ("NYNEX Petition for Waiver"), filed December 15, 1993. See also, Ad Hoc Opposition to NYNEX Petition for Waiver filed on January 31, 1994.

15. *U.S. v. AT&T*, Civil Action No. 82-0192; (D.D.C., 1983), July 8, 1983, as amended July 28, 1983, and August 5, 1983, 569 F. Supp. 1057 1097-1101. Citing an affidavit of William Weiss (then CEO-designate of Ameritech), Judge Green identified four categories of "Official Services" for which BOC-owned interLATA facilities may be used:

(1) The Operational Support System Network is a network of dedicated voice and data private lines used by the Operating Company to monitor and control trunks and switches. These communications links are vital to the proper operation of the network since, for example, they enable Operating Company personnel to measure the maintenance status of trunks and switches and instantly to control equipment and reroute traffic.

(2) The Information Processing Network is a network of dedicated data lines linking the Operating Companies' information system computer. It is used to transmit data relating to customer trouble reports, service orders, trunk orders from interexchange carriers, and other information necessary for carrying out

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